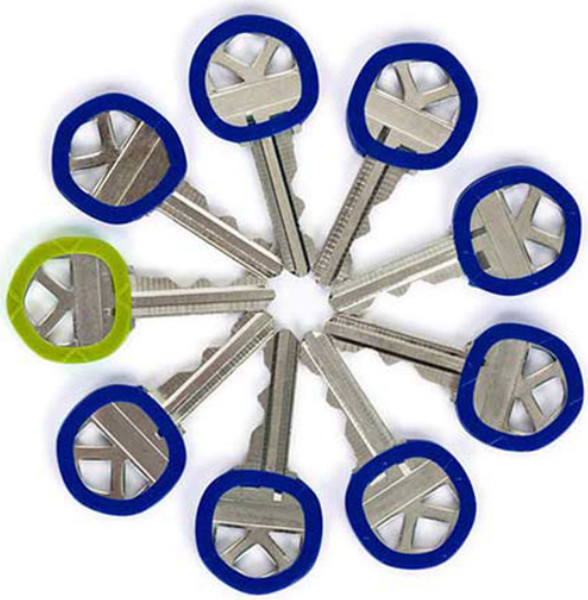
IRS Insights
A closer look.
May 2019



In this issue:

Tax Court rules on proper process for Taxpayer to change their "Last Known Address" with the IRS

In *Gregory v. Commissioner*,[1] the Tax Court held that taxpayers cannot change their last known address on file with the IRS by providing the new address on a Form 2848, *Power of Attorney and Declaration of Representative*, or a Form 4868, *Application for Automatic Extension of Time to File US Individual Income Tax Return*, because these forms are not tax returns and do not provide adequate notice of the address change to the Internal Revenue Service ("IRS").

[1] 152 T.C. No. 7 (Mar. 13, 2019).

Background

The taxpayers in *Gregory* erroneously used their old mailing address when they filed their 2014 income tax return.[2] Subsequently, the taxpayers submitted Forms 2848 that provided their new address.[3] The taxpayers also filed a Form 4868 that also provided their new address.[4]

Before the taxpayers filed their 2015 return, the IRS mailed a notice of deficiency for 2014 to the taxpayers' old address, which was not returned to the IRS and not delivered. The taxpayers did not discover that the IRS had issued to them a notice of deficiency until after the period for filing a petition with the US Tax Court expired.

Analysis

Under section 6212(b)(1), a notice of deficiency is only valid if it is sent to the taxpayer's last known address. Unless the IRS is given clear and concise notice of an address change, a taxpayer's last known address is the address that appears on a taxpayer's most recent Federal tax return.[5] Typically, taxpayers notify the IRS of an address change by filing a Form 8822, *Change of Address*. The taxpayers in *Gregory* did not do so.

After receiving a copy of the notice of deficiency, the taxpayers filed an untimely petition contesting the deficiency with the US Tax Court.[6] The IRS and the taxpayers each moved for dismissal for lack of jurisdiction. The IRS argued that the notice of deficiency was sent to the taxpayers' last known address because the Forms 2848 and Form 4868 were not returns and did not provide it with clear and concise notice of the address change. The taxpayers argued that the Forms 2848 and Form 4868 were returns and provided clear and concise notice of the address change to the IRS.

The court held that a Form 2848 and a Form 4868 are not returns under the test that it set forth in *Beard v. Commissioner*[7] because the forms do not provide any information necessary for the IRS to determine a tax liability and they do not purport to be returns.[8] Indeed, the court noted that Rev. Proc. 2010-16 expressly states that the Form 2848 and the Form 4868 are not returns.[9]

The court also held that the Forms 2848 and Form 4868 did not provide clear and concise notice of the address change to the IRS.[10] Thus, the court distinguished previous cases that held that including a new address on a Form 2848 provides clear and concise notice of an address change to the IRS.[11] In distinguishing those cases, the court noted that the instructions to both the current Form 2848 and the current Form 4868 provide that the forms will not change a taxpayer's address with the IRS.[12] By contrast, the instructions to previous versions of the Form 2848 did not contain this warning.[13]

Conclusion

Gregory illustrates the importance of ensuring that the IRS has a taxpayer's current address. Taxpayers should use a Form 8822 to notify the IRS of an address change. That is the best way to ensure that IRS notices are received on a timely basis.

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[2] *See Gregory*, 152 T.C. No. 7, Slip Op. at 2.
[3] *See id.*, Slip Op. at 3.
[4] *See id.*
[5] *See* Treas. Reg. § 301.6212-2(a).
[6] *See Gregory*, 152 T.C. No. 7, Slip Op. at 3.
[7] 82 T.C. 766 (1984).
[8] *See Gregory*, 152 T.C. No. 7, Slip Op. at 7-8.
[9] *See id.*, Slip Op. at 8.
[10] *See id.*, Slip Op. at 9-10.
[11] *See id.*, Slip Op. at 11-14 (discussing *Hunter v. Comm'r*, T.C. Memo. 2004-81, and *Expanding Envelope & Folder Corp. v. Shotz*, 385 F.2d 402 (3d Cir. 1967)).
[12] *See id.*, Slip Op. at 12.
[13] *See id.*

Court of Federal Claims rules that it lacked subject-matter jurisdiction where a taxpayer failed to sign its refund claim that was the basis for the taxpayer's refund suit

In *Wilson v. United States*,[14] the United States Court of Federal Claims dismissed a taxpayer's refund suit for lack of subject-matter jurisdiction because the taxpayer failed to properly sign its Form 843, Claim for Refund and Request for Abatement, that was the basis for its refund suit.

Facts

The IRS assessed a 35 percent penalty against the taxpayer pursuant to section 6677(a) for failure to file a Form 3520, Annual Return To Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts.[15] The taxpayer disputed the 35 percent penalty, arguing that a 5 percent penalty under section 6048(b) should have been imposed instead.[16] The taxpayer paid the penalty and filed a Form 843, Claim for Refund and Request for Abatement. The Form 843 was signed by the taxpayer's counsel, who was the taxpayer's authorized representative via Form 2848, Power of Attorney and Declaration of Representative. The authorized representative signed the Form in the "Paid Preparer Use" area. However, the signature area under penalties of perjury language was not signed by the taxpayer and it was left blank.

The taxpayer ultimately filed a complaint, based upon the Form 843 that it filed, seeking an abatement of a portion of the penalty and a refund of the excess penalty that was paid by the taxpayer. The Government filed a motion to dismiss for lack of subject-matter jurisdiction on the grounds that the Form 843 was invalid.

Law and Analysis

The taxpayer bears the burden of establishing subject matter jurisdiction. The standard for establishing subject-matter jurisdiction in a tax refund suit is set out in section 7422(a), which states that no suit or claim shall be maintained in any court for the recovery of tax allegedly to be erroneously assessed or collection until after a claim for refund is duly filed.[17]

The Government took the position that a taxpayer's signature of a claim for refund (*e.g.*, Form 843) under the penalty of perjury is jurisdictional and therefore, the claim for refund at issue was not duly filed and the complaint should be dismissed for lack of subject-matter jurisdiction. The Government argued that the signature of the tax return preparer cannot verify a refund under the penalties of perjury and the two signatures (that of the paid preparer and that of the taxpayer) serve different purposes.

In response, the taxpayer argued that the proper interpretation of Form 843 is that the return preparer's signature is incorporated under the penalty of perjury language. The taxpayer cited the language in Form 2848 that "declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge" as evidence that the tax preparer's signature alone can suffice and certify the taxpayer's refund claim as valid. The taxpayer's argument relied on the contention that the Form 2848, Power of Attorney, authorized a representative to file a refund claim on behalf of the taxpayer. The Government argued that because the taxpayer's Form 2848 did not contain a clear expression of the representative's scope of authority, the representative was, therefore, not explicitly authorized to file a claim for refund for the taxpayer.

The question before the court was whether the Form 2848 contained a clear expression of authority granting the representative the ability to sign the refund claim. The court observed that regulations makes a distinction between a

[14] No. 18-408T (Fed. Cl. Feb. 27, 2019)
[15] *See* § 6677(a)
[16] *See* § 6048(b)
[17] *See* § 7422(a)

preparer's and taxpayer's signature.[18] However, the regulations do not address whether a preparer, who also possesses a power of attorney, can sign as a paid preparer and satisfy the taxpayer's signature requirement.

In *Wilson*, the taxpayer's Form 2848 authorized the representative to perform all acts, including signing documents, with respect to civil penalties. The court observed that such documents included Form 843. In support of its position that the representative was authorized to sign Form 843 on its behalf, the taxpayer cited *Aronsohn v. Comm'r*, which held that a Form 2848 does not require a more specific authorization for making a claim for refund.[19] In *Aronsohn*, the Third Circuit affirmed the district court's holding that the Form 870-AD, Offer of Waiver of Restrictions on Assessment and Collections of Deficiency in Tax and Acceptance of Overassessment, did not require a more specific Form 2848.

The Government countered that *Arohnson* was not on point as that case did not address whether a Form 2848 authorized a representative to sign a document under penalty of perjury. The court noted that while the Form 2848 is silent on the matter of refunds it does have a specific box for taxpayers to check to authorize a representative to sign a return.

The court concluded that while refund claims and returns are different, the taxpayer failed to show why the Form 2848 would require a taxpayer to expressly indicate that their representative is empowered to sign a return under penalties of perjury but would not require any express indication for a refund claim, which is also signed under penalty of perjury. The court found that the taxpayer had not met his burden and demonstrated by a preponderance of the evidence that Form 2848 is a broad authorization that extends to signing a claim for refund under penalties of perjury.

The taxpayer also argued alternatively that the refund claim qualifies as an informal claim for refund. The taxpayer argued that the IRS recognizes the validity of informal claims despite not being signed under the penalties of perjury. The court was not persuaded by this argument. The court observed that the doctrine of informal claim, developed in *United States v Kales*, was devised to allow taxpayers to remedy a timely defective claim after the statute had lapsed.[20] In the present case, the taxpayer's ability to file a valid claim for refund is not time barred. The court decided that the taxpayer could not rely upon the informal claim doctrine to cure his refund claim and must instead file a duly filed claim for refund.

Tax Court Holds that Certain Penalties that are Determined and Calculated Electronically Do Not Require Supervisory Approval

In two recent cases, *Walquist v. Commissioner*[21] and *ATL & Sons Holdings, Inc. v. Commissioner*,[22] the Tax Court held that, when certain penalties are determined and calculated electronically without any involvement by IRS personnel, those penalties are exempt from the requirement, under section 6751(b), that written supervisory approval of the initial penalty determination be obtained before assessing the penalty.

Background

Under section 6751(b)(1), before a penalty, addition to tax, or additional amount is assessed, the immediate supervisor of an IRS employee determining to apply such penalty, addition to tax, or additional amount is required to approve the penalty, in writing. Penalties assessed under sections 6651, 6654, and 6655[23] and "any other penalty automatically calculated through electronic means"[24] are exempt from this requirement. In *Graev v. Commissioner*, ("*Graev III*"), the Tax Court held that written supervisory approval must occur no later than the date the IRS mails the notice of deficiency or files an answer or amended answer asserting penalties.[25]

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[18] See Treas. Reg. § 1.6695-1(b)(1)
[19] *Aronsohn v. Comm'r*, 988 F.2d 454,456 (3rd Cir. 1993)
[20] *United States v. Kales*, 314 US 186, 194 (1941)
[21] 152 T.C. No. 3 (Feb. 25, 2019).
[22] 152 T.C. No. 8 (Mar. 13, 2019).
[23] I.R.C. § 6751(b)(2)(A).
[24] I.R.C. § 6751(b)(2)(B) (emphasis added).
[25] 149 T.C. 485, 495 (2017) (citing *Chai v. Comm'r*, 851 F.3d 190, 221 (2d Cir. 2017)).

The penalty at issue in *Walquist* was determined under section 6662(b)(2). Section 6662(b)(2) imposes a 20% penalty on any substantial understatement of tax shown on a return. For an individual, an understatement is substantial if the understatement exceeds the greater of $5,000 or 10% of the tax required to be shown on the return.[26] The substantial underpayment penalty does not apply if the substantial underpayment was due to reasonable cause.[27]

The penalty at issue in *ATL & Sons* was assessed under section 6699(a). Section 6699(a) provides that an S corporation that fails to timely file its annual return is liable for a penalty for each month, or fraction of a month, during which such failure continues. The delinquency penalty for the years at issue was equal to $195 multiplied by the number of persons who were S corporation shareholders during the taxable year.[28] The delinquency penalty does not apply if the failure to file was due to reasonable cause.[29]

No court has previously addressed whether the substantial understatement penalty under section 6662(b)(2)(B) or the delinquency penalty under section 6699 can be considered "automatically calculated through electronic means."[30]

Walquist v. Commissioner

In *Walquist*, the IRS's Automated Correspondence Exam system, using the Correspondence Examination Automated ("CAES") software program, determined that the taxpayers were liable for a substantial understatement penalty under section 6662(b)(2).[31] CAES is designed to process cases "with minimal to no tax examiner involvement until a taxpayer reply is received."[32] After the taxpayers failed to reply to a 30-day letter, the IRS issued a notice of deficiency to the taxpayers that included a determination of the substantial understatement penalty by CAES. No human IRS examiner reviewed the substantial understatement penalty determined in the notice of deficiency.

The issue before the Tax Court was whether a substantial understatement penalty under section 6662(b)(2) can be considered a penalty that is "automatically calculated through electronic means" under section 6751(b)(2)(B). The court observed that both the application and the amount of the substantial underpayment penalty can be determined mathematically.[33] Because the substantial understatement penalty was mathematically determined by a computer software program without the involvement of any human IRS examiner, the court concluded that the penalty was exempt from the written supervisory approval requirement of section 6751(b)(1).

The court noted that its conclusion is supported by the statutory context. The exception for "any other penalty automatically calculated through electronic means"[34] follows the exception for "any addition to tax under section 6651, 6654, or 6655."[35] Like the additions to tax under sections 6651, 6654, and 6655, the substantial understatement penalty is mandatory, can be mathematically determined and applied, and is subject to a reasonable cause defense.

The substantial understatement penalty here also does not raise the same concerns as other penalties that are more discretionary. As the Second Circuit explained in *Chai v. Commissioner*, the supervisory approval requirement "was meant to prevent IRS agents from threatening unjustified penalties to encourage taxpayers to settle."[36] Because no human IRS employee reviewed the penalty determined in the notice of deficiency, it would be impossible for such unfair IRS employee conduct to occur. Thus, the court concluded that its holding is consistent with the congressional

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[26] I.R.C § 6662(d). In the case of any return required to be filed in 2019, the penalty is $200 multiplied by the number of persons who were S corporation shareholders during the taxable year. *See* Rev. Proc. 2017-58, § 3.50.
[27] I.R.C § 6664(c)(1).
[28] *See* I.R.C. § 6699(b).
[29] *See* I.R.C. § 6699(a).
[30] I.R.C. § 6751(b)(2)(B). The Tax Court previously held a section 6652(c) delinquency penalty for failure by a tax-exempt organization to file an annual return, *see Grace Found. v. Comm'r*, T.C. Memo. 2014-229, and a section 6702 penalty for filing a frivolous tax return, *see Lindberg v. Comm'r*, T.C. Memo. 2010-67, were exempt from the supervisory approval process because they were automatically calculated through electronic means.
[31] 152 T.C. No. 3, Slip Op. at 3-4.
[32] *Id.* (quoting IRM pt. 4.19.20.1.1 (Dec. 18, 2017)).
[33] *Walquist*, 152 T.C. No. 3, Slip Op. at 18.
[34] I.R.C. § 6751(b)(2)(B).
[35] I.R.C. § 6751(b)(2)(A).
[36] *Chai*, 851 F.3d at 219.

purpose in excepting penalties "automatically calculated through electronic means" from the supervisory approval requirement.[37]

ATL & Sons Holdings, Inc. v. Commissioner

In *ATL & Sons*, a collection due process case, an S corporation with two shareholders was assessed a penalty under section 6699 for failing to timely file its Form 1120S, *US Income Tax Return for an S Corporation*.[38] The assessment of the delinquency penalty appears on the taxpayer's account transcripts with a code indicating that the penalty is a "Computer generated assessment of Delinquency Penalty."[39] No supervisory approval of the delinquency penalty was obtained before the penalty was assessed.[40]

As in *Walquist*, the issue before the Tax Court was whether the delinquency penalty under section 6699 can be considered "automatically calculated through electronic means."[41] The court compared the delinquency penalty to the failure-to-file penalty under section 6651(a)(1).[42] Like the delinquency penalty, the failure-to-file penalty can be determined mathematically and is subject to a reasonable cause exception. As the delinquency penalty was assessed electronically, the court concluded that it was exempt from the supervisory approval requirement.[43]

Finally, the court explained that the reasonable cause exception does not prevent the delinquency penalty from being considered "automatically calculated through electronic means" because reasonable cause is an affirmative defense, which the taxpayer is obligated to raise.[44] Thus, the IRS can establish liability for the penalty before considering any reasonable cause defense that the taxpayer may later raise.[45] To support this conclusion, the court noted that almost all the penalties that are exempt from the supervisory approval requirement are subject to a reasonable cause defense.[46] Thus, it is evident that the existence of a potential reasonable cause defense does not preclude a penalty from being considered "automatically determined thorough electronic means" within the meaning of that term in section 6751(b)(2)(B).

Conclusion

Walquist and *ATL & Sons* clarify the scope of the "any other penalty automatically calculated through electronic means" exception to the written supervisory approval requirement of section 6751(b)(1). Taxpayers should be aware that penalties that are automatically calculated – including many failure-to-file and failure-to-pay penalties – will likely not be subject to the written supervisory approval requirement.

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[37] *Walquist*, 152 T.C. No. 3, Slip Op. at 18 – 19.
[38] 152 T.C. No. 8 (Mar. 13, 2019).
[39] *Id.*, Slip Op. at 4.
[40] *See id.*
[41] I.R.C. § 6751(b)(2)(B).
[42] *See* 152 T.C. No. 8, Slip Op. at 22 – 23.
[43] *See id.*, Slip Op. at 23 – 24.
[44] *See id.*, Slip Op. at 27. The court noted that the accuracy-related penalty for negligence under section 6662(b)(1) was not at issue in *ATL & Sons*. Thus, the court did not address whether the negligence penalty could be considered "automatically calculated through electronic means" under section 6751(b)(2)(B). *See id.*, Slip Op. at 26 n.7.
[45] *See id.*, Slip Op. at 28.
[46] *See id.*, Slip Op. at 27.

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